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For Immediate release - January 26, 2010

Governor Patrick Announces Next Phase of Pension Reform

Comprehensive changes place cap on earnings, raise retirement age to make system fair for taxpayers, state employees

BOSTON - Tuesday, January 26, 2010 - Building on sweeping pension reforms he signed into law last year that closed loopholes and eliminated abuses in the public retirement system, Governor Deval Patrick today filed his proposal to further overhaul the benefits plan to ensure its long-term sustainability and credibility. The Administration's plan, informed by the recommendations of the Special Commission on Pension Reform, calls for capping pension earnings, eliminating the so-called section 10 early retirement incentive and increasing retirement ages, among other proposals.
The Patrick-Murray Administration's Phase II pension reform legislation proposes to change the system to make it more fair and equitable for taxpayers and all state workers, while also making the system fiscally sustainable. Taken together, the reforms are expected to save taxpayers an estimated $2 billion over 30 years.

"We took an important step last year when we eliminated some of the most egregious abuses and delivered pension reforms that people had been talking about for years," said Governor Patrick. "The provisions included in this plan go further, and they are absolutely necessary to reinforce to the public that state government continues to be focused on their business and not on personal gain."

"This second phase of pension reform would ensure greater financial stability in the pension system and continue to restore the public's confidence in the fairness of the system," said Lieutenant Governor Timothy Murray.

Where constitutionally permissible, provisions will apply to current state employees. Where the state Constitution clearly prohibits law changes from impacting current employees those provisions will apply to all new employees.

Cap Earnings for Purposes of Calculating Benefits

The Patrick-Murray Administration's plan calls for capping maximum annual pension payments by limiting them to a percentage of the federal limit, which would currently result in a maximum pension benefit of $85,000. Employees will only contribute to the pension system up to the cap on regular compensation.

This cap on benefits, which is three times the median U.S. wage per person, will ensure that taxpayers are not responsible for contributing to excessive public pensions. The average state retiree, who does not receive Social Security benefits, receives a pension of about $26,000 a year, and less than one percent of current state retirees receive pensions in excess of $85,000.

Increased Retirement Age

The Patrick-Murray Administration's plan increases the retirement age for virtually all state workers, reflecting the fact that people are living and working longer than when the retirement ages were set in state law 60 years ago. The proposed changes are as follows:

- Group 1 (elected officials and most general employees): Increase the retirement age to 60-67 from the current 55-65;
- Group 2 (employees with titles reflecting hazardous duties): Increase the retirement age to 55-62 from the current 55-60;
- Group 4 (firefighters, police officers, some corrections officers): Increase the retirement age to 50-57 from the current 45-55.

Since 1950, overall life expectancy has increased 9.6 years. For Social Security benefits, the full retirement age is now 67 for people born after 1959. The current retirement ages for Groups 1 and 2 have not changed since 1957 and do not account for this life expectancy increase. Group 4, added to the system in 1967, is also out of date. In addition to raising the retirement ages, the

Administration's plan would reduce the existing subsidy for employees retiring at younger ages.

Eliminate Section 10 Early Retirement Incentive for All Employees

Pension Reform Phase I eliminated the so-called section 10 early retirement incentive for elected officials. The Phase II proposal eliminates the perk for all employees, not just elected officials. Currently, employees with 20 years of service who are terminated at no fault of their own - usually as a result of a change in Administrations - are entitled to an early retirement benefit equal to 1/3 of their highest three earning years plus an annuity from contributions. In most cases, that lifetime termination benefit is significantly larger than what the employee would have received if not terminated and declines with further increases in age and service.

Other proposals included in Pension Reform Phase II include:

Pro-Rate Benefits Based on Employment History

The Patrick-Murray Administration's plan calls for pro-rating the retirement allowance for employees who have served in more than one Group, taking into account the number of years of service in each group. The current retirement allowance is based on benefits of the Group of which an employee is a member at their time of retirement, even if the employee has spent the majority of their career in a Group with lesser benefits. Pro-rating prevents windfalls for people who have only a short period of service in a Group with higher benefit levels.

Anti-Spiking

The Patrick-Murray Administration's plan introduces an anti-spiking rule, limiting the annual increase in pensionable earnings to no more than 7 percent plus inflation of the average pensionable earnings over the previous two years. This provision would not apply for bona fide promotions or job changes.

Increase "High 3" to "High 5 "

The Patrick-Murray Administration's plan also calls for increasing the period for averaging earnings for purposes of calculating a member's retirement allowance from 3 to 5 years. A slightly longer averaging period more accurately reflects an employee's career earnings.

The Patrick-Murray Administration's plan also calls for the following common sense, cost-saving initiatives:

- Requiring Supreme Court Justices, the only state employees who do not currently contribute to the retirement system, to contribute to their benefits;
- Increasing scrutiny of legislation benefiting individual employees by requiring such legislation to be accompanied by an actuarial cost estimate, confirmation of the cost analysis from the Public Employees Retirement Commission and a recommendation from the Retirement Board;
- Requiring elected officials to repay the full value of the pension they have received in order to rejoin the system, consistent with what all other state employees are required to do;
- Requiring members who rejoin the system or new members eligible to receive creditable service based on work elsewhere to purchase creditable service within one year or pay the full actuarial interest rate;
- Allowing retirement boards to require retirees convicted of a criminal offense related to their employment to repay benefits received since the date of the offense, not just the date of conviction;
- Allowing retirement boards to withhold the processing of pension benefits for retirees charged with an offense relating to their employment;
- Charging retiree health insurance to prior employers based on the portion of an employee's service in each jurisdiction, similar to the provision for pensions; and
- Reducing the employee contribution level for new Group 1 employees who will be subject to the restructured benefit system to ensure that employees do not contribute more into the pension system than they are likely to receive in benefits.

"The thoughtful changes in this legislation strike the right balance between providing our state workforce with retirement benefits they can depend on and ensuring that taxpayers are not responsible for paying for overly-generous pensions," said Administration and Finance Secretary Jay Gonzalez. "The changes the Governor is proposing will ensure the public employee pension system is fair, credible and fiscally sustainable."

The first phase of pension reform passed last year targeted glaring loopholes that had allowed some to exploit the system and unfairly boost their public pensions. Those changes were made applicable to both current and future state employees. Among the loopholes the law closed was the so-called "one day, one year" provision that allowed elected officials to claim an entire year of credible service for working one day in a calendar year. The law also removed a provision that allowed elected officials to claim a "termination allowance" based on the failure to be nominated or re-elected.

It is constitutionally permissible to apply the following new provisions to current and future state employees: pro-rating benefits based on group history; limiting annual increases on retirement earnings (anti-spiking); requiring members who re-enter the system to purchase creditable service within one year or pay a higher interest rate; collecting pension payouts from convicted retirees; increasing scrutiny of individual retirement legislation; and charging retiree health insurance to prior employers. All other provisions apply to new employees only.

The Commonwealth's public employee retirement system is a defined benefit plan that provides retirement and disability benefit levels similar to those of other states with defined benefit plans and no Social Security coverage for public employees.

The legislation as filed can be found here: Providing for the Modernization and Sustainability of the Pension System

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